Negative Testimony on SB 33
Tax Cuts for Retirement Income

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Background and Summary:

I have served as the chief academic adviser to the Governor's Tax Reform Council starting in 2019. The *Governor's Council on Tax Reform Final Report* discussed the recent history of taxation in Kansas, including the consequences of the Brownback Income tax cuts. This testimony draws upon these lessons.

This testimony is **Negative** on Senate Bill 33 because it eliminates taxes on retirement income and will reduce revenues for the state general fund.

Kansas completely exempts Social Security income from taxation for most senior tax-payers. Kansas employs a taxable-nontaxable switch for Social Security income. If federal adjusted gross income (AGI) is less than or equal to $75,000, none of the Social Security payment is taxable. If AGI exceed $75,000, the amount of Social Security taxable at the federal level is also taxable in Kansas. A difference of even $1 in federal AGI can mean a difference of several thousand dollars in Kansas AGI. The sudden jump in Kansas AGI income is known as a tax "cliff." A tax cliff will exist for any AGI cutoff level because the Kansas tax system does not ease in the taxability of Social Security income.

Table 6.4 reproduced from the *Governor's Council on Tax Reform Final Report* illustrates this Social Security tax cliff using hypothetical senior households. Clearly the legislature should consider adjustments to ameliorate or eliminate the Social Security tax cliff.

Table 6.4. *Federal and Kansas Taxable Social Security for Hypothetical Senior Households.*

Total Income ($)	Social Security income ($)	Social Security as % Total Income	Federal Taxable Social Security ($)	Kansas Taxable Social Security ($)	Federal AGI ($)	Kansas AGI ($)
25,000	19,000	76.0%	0	0	6,000	6,000
45,000	25,000	55.6%	250	0	20,250	20,000
80,000	30,000	37.5%	23,850	0	73,850	50,000
100,000	30,000	30.0%	25,500	25,500	95,500	95,500

Source: IPSR Hypothetical Taxpayer Model, Institute for Policy & Social Research, the University of Kansas.

However, SB 33 has become a virtual Christmas wish-list of tax cuts for senior households. In addition to eliminating all taxes on Social Security at a cost to the State General Fund of $117 million in FY 2025, the bill exempts all retirement income from taxation at a cost of $267 million in FY25, and includes changes to the Homestead provisions at a cost of $13.2 million. Additional provisions in the bill bring the grant total cost in FY 2025 to $441 million.

First, recent Kansas history illustrates the danger of extreme tax cuts like SB 33. When combined with SB 169 ($568 million), the total tax cuts proposed are in excess of $1 billion by FY 2025.

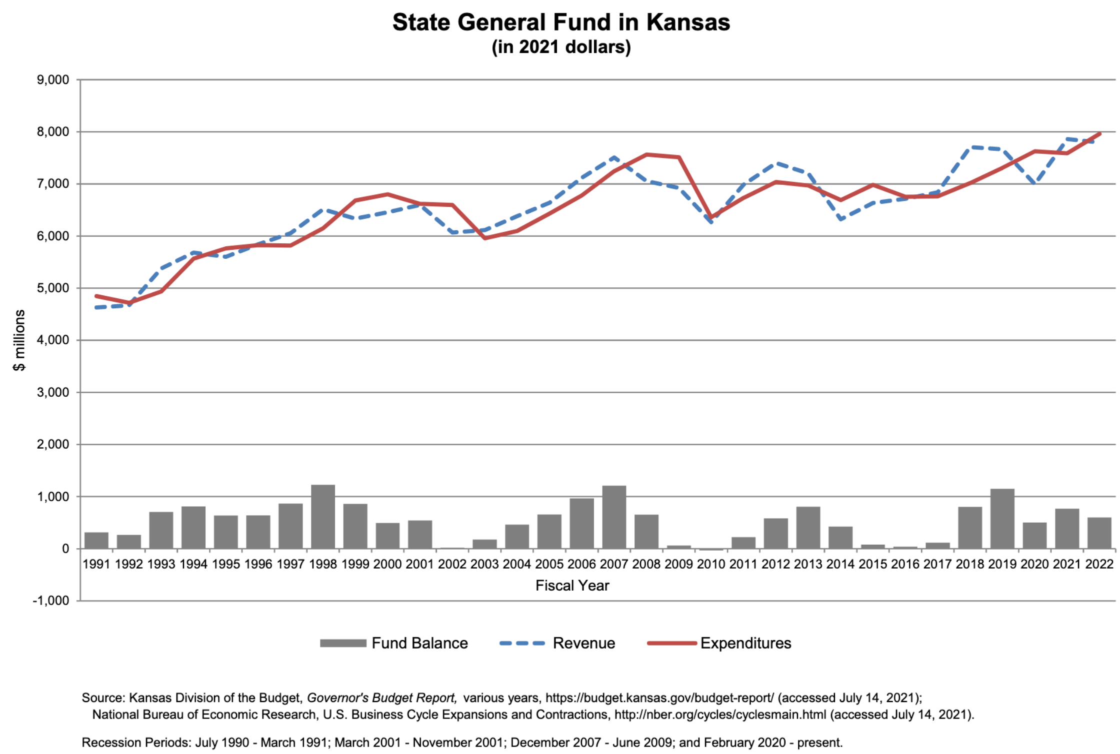

Figure 1: State General Fund Balances, Revenue and Expenditures. Source: The *Governor's Council on Tax Reform Final Report.*

Figure 1, reproduced from the *Governor's Council on Tax Reform Final Report* shows the precipitous decline in the State General Fund after 2014 due to the Brownback Tax Cuts. Beginning in 2014, expenditures outstripped revenues and by 2017, the Brownback tax cuts were largely reversed. Given the problems with the State General Fund, to balance the budget, the Governor and Legislature would "raid the bank of KDOT" by eliminating previously scheduled transfers from the SGF to support the state's transportation program. Kansas ranks fourth in the nation in terms of roads and highways. It is estimated that as much as $2.6 billion dollars was swept from the Kansas Department of Transportation (KDOT) budget to pay for the Brownback tax cuts.[1] It took four years for Governor Kelly to finally close the bank of KDOT.

[1] https://www.cjonline.com/story/news/politics/state/2019/01/18/gov-laura-kelly-offers-plan-to-gradually-downsize-bank-of-kdot/6255101007/

Second, the flat tax benefits the very top earners in Kansas compared to those with average income or below. Figure 2 shows the average tax cut by taxable income bracket for married couples filing jointly. The top 5% of married couples filing jointly (with Kansas taxable income in excess of $300,000 per year) receive an average annual tax cut of $8,439. This makes up 51.1% of the total tax cut from SB 169. The bottom 50% of married couple households filing jointly receive only 10.9% of the total tax cut. Thus, the flat tax favors the richest of filers in the state.

Third, there is no evidence that tax cuts like the flat tax or the Brownback tax cut lead to economic growth. Many economists have analyzed the economic impact of the Brownback tax cuts. DeBacker, Heim, Tramnath and Ross (2019) found no evidence that the Brownback tax cuts resulted in increased economic activity. Turner and Blagg (2018) examined whether the tax cuts resulted in increases in employment compared to states that did not enact tax cuts. They found that tax cuts did not result in any net increase in private-sector employment. Tax and budget policy analysts from groups as diverse as the Tax Foundation and the Center2 for Budget and Policy Priorities3 agreed that the "Tax Experiment" in Kansas was a failure in public policy. Furthermore, these tax cuts put Kansas' improved credit rating at risk, ultimately increasing debt service costs and costing Kansans more money.

While it is clear that the Social Security cliff needs to be addressed, the additional tax cuts on retirement income make this bill fiscally untenable. If we then combine the SB 33 tax cuts with those in SB 169, the price tag to the State General fund exceeds $1 billion per year. Kansas cannot afford these extreme tax cuts that lead to fiscal instability in the state.

A viable alternative to SB 33 would be HB 2109. This bill gradually exempts all Social Security income, and has a much smaller fiscal impact on the State General Fund.

References:

Jason DeBacker, Bradley T. Heim, Shanthi P. Ramnath, Justin M. Ross, "The impact of state taxes on pass-through businesses: Evidence from the 2012 Kansas income tax reform," in *Journal of Public Economics* 174 (June 2019): 53-75. https://doi.org/10.1016/j.jpubeco.2019.03.008 5

Tracy M. Turner and Brandon Blagg, "The Short-term Effects of the Kansas Income Tax Cuts on Employment Growth," in *Public Finance Review* 46; 6 (November 2018): 1024-1043. https://doi.org/10.1177/1091142117699274

Governor's Council on Tax Reform Final Report. https://ipsr.ku.edu/CSTEP/PDF/Tax_Council_Final_April2022.pdf.

[2] https://taxfoundation.org/every-tax-cut-kansas/

[3] https://www.cbpp.org/research/state-budget-and-tax/kansas-provides-compelling-evidence-of-failure-of-supply-side-tax